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10 **UNITED STATES DISTRICT COURT**
11 **SOUTHERN DISTRICT OF CALIFORNIA**
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13 TETRAVUE INC., et al.,
14 Plaintiffs,
15 v.
16 ST. PAUL FIRE & MARINE
17 INSURANCE COMPANY,
18 Defendant.
19

And Related Counter-Claim.
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Case No.: 14-CV-2021 W (BLM)

ORDER:

(1) **GRANTING PLAINTIFFS’
MOTIONS TO FILE DOCUMENT
UNDER SEAL [DOCS. 66, 77];**
(2) **GRANTING DEFENDANT’S
MOTION TO FILE DOCUMENTS
UNDER SEAL [DOC. 73];**
(3) **DENYING PLAINTIFFS’
SUMMARY-JUDGMENT MOTION
[DOC. 65]; AND**
(4) **GRANTING IN PART AND
DENYING IN PART DEFENDANT’S
SUMMARY-JUDGMENT MOTION
[DOC. 70]**

25 Pending before the Court are cross motions for summary judgment in this
26 insurance-coverage dispute. Plaintiffs Tetravue, Inc. and Paul Banks’ motion seeks
27 summary judgment on Defendant St. Paul Fire & Marine Insurance Company’s
28 counterclaim for reimbursement under Buss v. Superior Court, 16 Cal. 4th 35 (1997), and

1 declaratory relief. (*Pls' MSA Notice* [Doc. 65] 2:2–14.) Defendant's motion seeks
2 summary adjudication regarding Plaintiffs' bad-faith claim, as well as various damage
3 claims. (*Def's MSA Notice* [Doc. 70] 1:5–3:10.) In addition to these motions, the parties
4 have each filed motions to seal certain documents.

5 The Court decides the matters on the papers submitted, and without oral argument.
6 See CivLR 7.1.d. For the reasons discussed below, the Court **GRANTS** Plaintiffs' and
7 Defendant's motions to file documents under seal [Docs. 66, 73, 77], **DENIES** Plaintiffs'
8 summary-judgment motion [Doc. 65] and **GRANTS IN PART** and **DENIES IN PART**
9 Defendant's summary-judgment motion [Doc. 70].

10 11 **I. BACKGROUND**

12 This insurance-coverage dispute arises from an underlying lawsuit filed by
13 Plaintiff Paul Banks against his former employer, General Atomics ("GA"), in 2009.
14 (*Compl.* ¶ 12.¹) In April 2010, GA filed a cross complaint against Banks and Plaintiff
15 Tetravue, Inc., a company Banks founded after leaving GA. (*Id.* ¶¶ 12–13.) GA alleged
16 Banks founded Tetravue "in order to improperly exploit the technology, business plans
17 and strategy and other trade secret information [Banks] misappropriated from GA." (*GA*
18 *Amend. Cross-Compl.* ¶ 1.²) GA also accused Banks and Tetravue of "other wrongful
19 conduct... not involving GA's trade secrets, but, rather, with respect to their misuse of
20 GA's confidential non-trade secret information or physical property." (*Id.*)

21 On January 6, 2011, Tetravue tendered its defense of GA's cross action to
22 Defendant St. Paul, which had issued a commercial general liability policy to Tetravue,
23 effective December 15, 2009. (*See Policy.*³) The policy provided coverage for, among
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26 ¹ The Complaint is attached to the Notice of Removal [Doc. 1] as Ex. A.

27 ² GA's Amended Cross Complaint is attached to Plaintiffs' tender letter, which is attached to Sarnecky's
28 declaration [Doc. 65-2] as Ex. 2, and Collins' declaration [Doc. 70-3] as Ex. 2.

1 other things, property damage and advertising injury, defined as “injury, other than
2 bodily injury or personal injury, that’s caused by an advertising injury offense.” (*Id.* pp.
3 087–088.) An “advertising injury offense” included the “[u]nauthorized use of any
4 advertising material, or any slogan or title, of others in your advertising.” (*Id.* p. 088.)
5 The policy also excluded coverage for intellectual-property claims, but consistent with
6 the advertising-injury coverage, included an exception for,

7 ...advertising injury that results from the unauthorized use of any:

- 8 • copyrighted advertising material;
 - 9 • trademarked slogan; or
 - 10 • trademarked title;
- of others in your advertising.

11 (*Id.* p. 103.) Included with Plaintiffs’ tender letter was a copy of GA’s Amended Cross-
12 Complaint. (*See Sarnecky Decl. Ex. 2; Collins Decl. Ex. 2.*)

13 St. Paul assigned Plaintiffs’ claim to technical specialist Bill Collins on January 10,
14 2011, who analyzed the Amended Cross-Complaint for coverage. (*Collins Decl.* ¶5.)
15 Collins believed the allegations did not involve claims falling within the policy’s
16 coverage provisions, and also believed several exclusions applied, including the
17 intellectual-property exclusion. (*Id.* ¶ 5.) After analyzing the cross-complaint on the
18 morning of January 11, Collins called Neil Greenstein, the attorney who sent the tender
19 letter on behalf of Plaintiffs, and explained his coverage analysis. (*Id.* ¶ 6.) Greenstein
20 responded that he believed GA’s conversion cause of action created a potential for
21 coverage under the policy’s property-damage-coverage provision. (*Id.*)

22 Collins considered Greenstein’s contention about the property-damage provision,
23 but concluded there was no potential coverage because the alleged conversion of GA’s
24 property (1) was intentional, not accidental, and (2) pre-dated the inception of the policy.
25 (*Collins Decl.* ¶ 7.) On January 25, Collins sent a letter denying Plaintiffs’ defense
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28 ³ The Policy is attached to Collins’ declaration as Ex. 1. Unless otherwise indicated, page citations are
to the parties’ exhibit-page numbers.

1 tender. (*Id.* Ex. 4.) The letter also invited Plaintiffs to provide any additional
2 information “that may bear upon our coverage decision[.]” (*Id.* Ex. 4 at p. 241.)

3 On February 2, 2011, Greenstein requested that St. Paul reconsider its coverage
4 position under the policy’s property-damage and advertising-injury provisions. (*Collins*
5 *Decl.* Ex. 5 at p. 245.) In reconsidering its position, Collins consulted with in-house
6 counsel. (*Id.* ¶ 8.) On February 11, Collins e-mailed Greenstein and informed him that
7 St. Paul’s coverage position remained unchanged and that a formal response would
8 follow. (*Id.*)

9 On February 24, 2011, Plaintiffs filed a lawsuit for declaratory relief against St.
10 Paul in the San Diego Superior Court (the “Declaratory Relief Action”). (*See Dec. Relief*
11 *Compl.*⁴) On February 25, 2011, Greenstein e-mailed Collins a copy of the Declaratory
12 Relief Complaint. (*Collins Decl.* ¶ 9, Ex. 3 at p. 230.) From March 16 to March 23,
13 Collins exchanged emails with Greenstein and Robert Vantress, another attorney for
14 Plaintiffs, in which the parties staked-out their respective coverage positions. (*Id.* ¶¶ 10–
15 13, Exs. 7–11.)

16 Eventually, Plaintiffs and St. Paul filed cross-motions for summary judgment in the
17 Declaratory Relief Action. On September 9, 2011, the Superior Court granted St. Paul’s
18 motion and denied Plaintiffs’ motion. (*See Brooks Decl.* Ex. 20.) The court found that
19 an advertising-injury claim could not be fairly inferred from GA’s Amended Cross-
20 Complaint because the material that Banks allegedly stole and used was expressly alleged
21 to be trade secret and confidential information. (*Id.* Ex. 20 at p. 26.) The court also
22 found no coverage under the property-damage provision because the loss of use of the
23 allegedly stolen property (1) occurred before the policy’s inception, and (2) did not result
24 from an “accident.” (*Id.* Ex. 20 at pp. 26–27.)

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28 ⁴ The Declaratory Relief Complaint is attached to Brooks’ declaration [Doc. 70-2] as Ex. 19.

1 Plaintiffs appealed the order. On July 19, 2013, the Court of Appeal reversed,
2 finding that an advertising-injury claim could be inferred from GA's Amended Cross-
3 Complaint and thus a duty to defend existed. (*See Ct. App. Decision.*⁵) St. Paul did not
4 appeal, and on August 16, 2013, it agreed to defend Plaintiffs. (*Collins Decl.* ¶ 14, Ex.
5 12.) Thereafter, St. Paul paid \$2,379,443.67 to Plaintiffs or their attorneys. (*Id.* ¶¶ 15–
6 16, Exs. 13–15.) These payments included interest and \$88,500 for the value of Banks'
7 time allegedly spent defending the cross-action. (*Id.* ¶¶ 17–18, Ex. 16.)

8 Meanwhile, Plaintiffs prevailed in both the cross-action, and the affirmative claims
9 against GA, for which Plaintiffs were awarded \$7,782,090.23. (*Sautter Decl.* [Doc. 70-4]
10 ¶ 6.) This triggered a 12% “success fee” provision in Plaintiffs’ fee agreement with their
11 defense attorneys. (*Id.*) In June 2015, Plaintiffs requested St. Paul pay the “success fee”
12 in the amount of \$933,850.83 to their defense attorneys as an additional covered defense
13 cost, which St. Paul agreed to do. (*Id.* Ex. 17; *Collins Decl.* Ex. 14.)

14 On June 13, 2014, Plaintiffs filed this lawsuit against St. Paul in the San Diego
15 Superior Court, asserting causes of action for Breach of the Duty to Defend, and Breach
16 of Contract and Implied Covenant. On August 28, 2014, St. Paul removed the case to
17 this Court and eventually filed a counterclaim for Buss reimbursement and declaratory
18 relief. The parties have now filed cross-motions for summary judgment.

19 20 **II. MOTIONS TO SEAL EXHIBITS**

21 Plaintiffs have filed a motion to file an unredacted version of GA's Amended
22 Cross-Complaint under seal. The document is filed in support of Plaintiffs’ summary-
23 judgment motion. Plaintiffs contend the document contains information related to highly
24 sensitive, confidential, and/or trade secret information belonging to General Atomics or
25 the U.S. government, developed pursuant to government defense contracts, and was also
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28 ⁵ The Court of Appeal's decision is attached to Brooks' declaration as Ex. 22, and Sarnecky's
declaration as Ex. 6. Page citations are to the court's decision, not the parties' exhibit-page numbers.

1 sealed by the court in the underlying action. (*Pls' Mt. to Seal in Support of MSJ* [Doc.
2 66] 2:13–18.) St. Paul has not opposed the motion. Good cause appearing, the Court will
3 grant Plaintiffs' motion to seal.

4 Plaintiffs have also filed a motion to seal various documents referenced in their
5 opposition to St. Paul's summary-judgment motion.⁶ The documents include information
6 related to highly sensitive, confidential, commercial information belonging to Tetravue
7 and its investors, and have been designated Confidential under the Protective Order
8 entered in this case. (*Pls' Mt. to Seal in Support of. Opp'n* [Doc. 77] 2:12–16.) In
9 addition, Plaintiffs seek to seal other documents containing information related to highly
10 sensitive, confidential, and/or trade secret information belonging to General Atomics or
11 the U.S. government, developed pursuant to government defense contracts, and which
12 were subject to a protective order or sealed by the court in the underlying action. (*Id.*
13 2:16–22.) St. Paul has not opposed the motion. Good cause appearing, the Court will
14 grant Plaintiffs motion' to seal.

15 St. Paul has also filed a motion to seal a number of documents filed with their
16 opposition to Plaintiffs' summary-judgment motion. The documents and transcripts were
17 designated as confidential/highly confidential in the underlying action, and/or were
18 designated as confidential in this action because they contain information or testimony
19 about sensitive, confidential, and/or trade secret information belonging to Tetravue,
20 General Atomics, or the United States government, developed pursuant to defense
21 contracts. (*Def's Mt. to Seal* [Doc. 73] 7:3–8.) Plaintiffs have not opposed the motion.
22 Good cause appearing, the Court will grant St. Paul's request.

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⁶ The documents are also referenced in Plaintiffs' opposition to St. Paul's motion in limine.

1 **III. APPLICABLE LAW**

2 **A. Summary-judgment standard**

3 Summary judgment is appropriate under Rule 56(c) where the moving party
4 demonstrates the absence of a genuine issue of material fact and entitlement to judgment
5 as a matter of law. See Fed.R.Civ.P. 56(c); Celotex Corp. v. Catrett, 477 U.S. 317, 322
6 (1986). A fact is material when, under the governing substantive law, it could affect the
7 outcome of the case. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248 (1986). A
8 dispute about a material fact is genuine if “the evidence is such that a reasonable jury
9 could return a verdict for the nonmoving party.” Id. at 248.

10 A party seeking summary judgment always bears the initial burden of establishing
11 the absence of a genuine issue of material fact. Celotex, 477 U.S. at 323. The moving
12 party can satisfy this burden in two ways: (1) by presenting evidence that negates an
13 essential element of the nonmoving party’s case; or (2) by demonstrating that the
14 nonmoving party failed to make a showing sufficient to establish an element essential to
15 that party’s case on which that party will bear the burden of proof at trial. Id. at 322–23.
16 “Disputes over irrelevant or unnecessary facts will not preclude a grant of summary
17 judgment.” T.W. Elec. Serv., Inc. v. Pac. Elec. Contractors Ass’n, 809 F.2d 626, 630
18 (9th Cir. 1987). If the moving party fails to discharge this initial burden, summary
19 judgment must be denied and the court need not consider the nonmoving party’s
20 evidence. Adickes v. S.H. Kress & Co., 398 U.S. 144, 159–60 (1970).

21 If the moving party meets this initial burden, the nonmoving party cannot avoid
22 summary judgment merely by demonstrating “that there is some metaphysical doubt as to
23 the material facts.” In re Citric Acid Litig., 191 F.3d 1090, 1094 (9th Cir. 1999) (citing
24 Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574, 586 (1986); Triton
25 Energy Corp. v. Square D Co., 68 F.3d 1216, 1221 (9th Cir. 1995) (citing Anderson, 477
26 U.S. at 252) (“The mere existence of a scintilla of evidence in support of the nonmoving
27 party’s position is not sufficient.”). Rather, the nonmoving party must “go beyond the
28 pleadings and by her own affidavits, or by ‘the depositions, answers to interrogatories,

1 and admissions on file,’ designate ‘specific facts showing that there is a genuine issue for
2 trial.’” Ford Motor Credit Co. v. Daugherty, 279 Fed. Appx. 500, 501 (9th Cir. 2008)
3 (citing Celotex, 477 U.S. at 324). Additionally, the court must view all inferences drawn
4 from the underlying facts in the light most favorable to the nonmoving party. See
5 Matsushita, 475 U.S. at 587.

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7 **B. California insurance law**

8 California law obligates an insurer to defend the insured when the facts alleged in
9 the complaint create a potential for coverage. Scottsdale Ins. Co. v. MV Transp., 36 Cal.
10 4th 643, 654 (2005). However, in evaluating the duty to defend, the insurer may also
11 consider facts outside those alleged in the complaint. Id. “If any facts stated or fairly
12 inferable in the complaint, or otherwise known or discovered by the insurer, suggest a
13 claim potentially covered by the policy, the insurer’s duty to defend arises and is not
14 extinguished until the insurer negates all facts suggesting potential coverage.” Horace
15 Mann Ins. Co. v. Barbara B., 4 Cal. 4th 1076, 1081 (1993). Thus, [i]n a declaratory relief
16 action to determine the duty to defend, ‘the insured need only show that the underlying
17 claim *may* fall within policy coverage; the insurer must prove it *cannot*.” State Farm v.
18 Superior Court, 164 Cal. App. 4th 317, 323 (2008 (citing Montrose Chemical Corp. v.
19 Superior Court, 6 Cal. 4th 287, 300 (1993))).

20 Bad faith occurs where the insurer withholds insurance benefits unreasonably and
21 without proper cause. Rappaport-Scott v. Interinsurance Exch. Of the Automobile Club,
22 146 Cal. App. 4th 831, 837 (2007). Absent unreasonableness, the insurer’s failure to
23 defend gives rise only to contract damages:

24 A breach of the duty to defend in itself constitutes only a breach of contract,
25 but it may also violate the covenant of good faith and fair dealing where it
26 involves unreasonable conduct or an action taken without proper cause. On
27 the other hand, if the insurer’s refusal to defend is reasonable, no liability
28 will result.

1 Shade Foods, Inc. v. Innovative Products Sales & Marketing, Inc., 78 Cal. App. 4th 847,
2 881 (2000).

3 In Wilson v. 21st Century Ins. Co., 42 Cal. 4th 713 (2007), the California Supreme
4 Court explained that bad faith does not lie with “an honest mistake, bad judgment or
5 negligence, but rather by a conscious and deliberate act, which unfairly frustrates the
6 agreed common purposes and disappoints the reasonable expectations of the other party
7 thereby depriving that party of the benefits of the agreement.” Id. at 726 (quoting
8 Chateau Chamberay Homeowners Assn. v. Associated Internat. Ins. Co., 90 Cal. App. 4th
9 335, 346 (2001)). Thus, bad faith may lie where a claim is denied “on a basis unfounded
10 in the facts known to the insurer, or contradicted by those facts” or where the insurer
11 ignores evidence that supports the insured’s claim, and just focuses on facts that justify
12 denial. Id. at 722.

14 **IV. DISCUSSION - DEFENDANT’S MOTION**

15 **A. The Bad-Faith Claim**

16 St. Paul seeks summary adjudication of Plaintiffs’ bad-faith cause of action.
17 Resolution of this issue turns on whether St. Paul’s position that GA’s Amended Cross
18 Complaint did not allege a potential advertising-injury claim was unreasonable. For the
19 reasons that follow, the Court finds the undisputed facts establish that St. Paul’s position
20 was not unreasonable.

21 The policy obligated St. Paul to “pay amounts” that Plaintiffs were “obligated to
22 pay as damages for covered advertising injury that:”

- 23 • results from the advertising of your products, your work, or your
24 completed work; and
- 25 • is caused by an advertising injury offense committed while this
26 agreement is in effect.

27 (*Policy* p. 087.) The policy defined an “advertising injury” as an “injury, other than
28 bodily injury or personal injury, that’s caused by an advertising injury offense.” (*Id.* p.

1 088.) Relevant to this case, an “advertising injury offense” included the “[u]nauthorized
2 use of any advertising material, or any slogan or title, of *others* in your advertising.” (*Id.*,
3 italics added.) “[A]dvertising” meant “attracting the attention of others by any means for
4 the purpose of” either “seeking customers or supporters” or “increasing sales or
5 business,” and “advertising material” meant “any covered material that: [¶] is subject to
6 copyright law; and [¶] others use and intend to attract attention to their advertising.” (*Id.*)

7 Based on these provisions, in order for there to be a potential for coverage under
8 the advertising-injury-liability provision, GA’s Amended Cross-Complaint must allege or
9 include facts from which it may be inferred that:

- 10 (1) Plaintiffs took material that GA *itself* used and intended to attract the
11 attention of others by any means for the purpose of seeking customers or
12 supporters or for increasing its sales or business;
13 (2) the material in question is subject to copyright law; and
14 (3) an accusation by GA that Plaintiffs used or were using that material to
15 attract the attention of others for the purpose of seeking customers or
16 supporters, or for the purpose of increasing sales or business.

17 (*Ct. App. Decision* p. 12, emphasis in original.)

18 In its motion, St. Paul does not dispute that the Amended Cross-Complaint’s
19 allegations satisfied the second and third elements. Instead, St. Paul contends it
20 reasonably believed there were no allegations satisfying the first element because the
21 cross-action had nothing “to do with GA’s own advertising materials.” (*Def’s P&A*
22 [Doc. 70-1] 20:5–7.) The undisputed fact support St. Paul’s position.

23 To begin with, as Plaintiffs acknowledge, there is no dispute that GA’s Amended
24 Cross-Complaint was long and complex, consisting of “187 charging paragraphs,” and
25 involving “high level technology.” (*Pls’ Opp’n* [Doc. 76] 3:11–16.) Also undisputed is
26 that nowhere in the long and complex cross complaint does GA explicitly allege
27 Plaintiffs took material that GA *itself* used in advertising or to attract the attention of
28 others for the purpose of seeking customers or supporters or for increasing its sales or
business. (*See GA Amend. Cross-Compl; Def’s P&A* 20:5–7.) Indeed, the California

1 Court of Appeal acknowledged “the absence of express allegations in the cross-complaint
2 that General Atomics used the relevant materials to ‘attract the attention of others’....”
3 (*Ct. App. Decision* p. 21.) In short, these allegations indicate that a certain degree of
4 difficulty existed in determining the cross-action involved GA’s advertising material.

5 Not only did the Amended Cross-Complaint omit an allegation that the materials
6 Banks’ took involved GA advertising material, but the parties’ communications indicate
7 they were unaware of allegations that created such an inference. Between January 11,
8 2011 and March 23, 2011, there were numerous emails exchanged between Plaintiffs’
9 attorneys and St. Paul. (*Collins Decl.* ¶¶ 6–13.) At no time during these communications
10 did Plaintiffs’ attorneys point to any allegations from which it could be inferred that the
11 material Banks took was used by GA in its advertising, to attract the attention of others
12 outside GA, or to increase its business. (*Id.* ¶ 6, Exs. 3, 5, 8, 11.) Particularly significant
13 are communications between Collins and Vantress between March 18 and March 23,
14 when the parties began to focus attention on the advertising-injury provision. On March
15 18, Collins specifically informed Vantress that St. Paul did not believe the lawsuit
16 involved the unauthorized use of GA’s advertising material:

17 Nothing in the complaint alleges a covered advertising injury arising from an
18 advertising injury offense (the elements of which are explained in the plain
19 language of the policy also cited in my letter). The Cross-Complaint alleges
20 the misappropriation of trade secrets and breach of confidentiality
21 agreements, *not the unauthorized use of General Atomics “advertising*
22 *material”*.

23 (*Collins Dec.* ¶ 11, Ex. 9 at 260, emphasis added.) On March 22, Collins followed up by
24 requesting from Plaintiffs,

25 [a]ll documents showing that General Atomics seeks damages for covered
26 “advertising injury” to include *any materials showing that GA pursues*
27 *claims for damages resulting from Tetravue’s unauthorized use of General*
28 *Atomic’s “advertising material” instead of ideas and/or trade secrets*. This
would include any documents demonstrating that unauthorized injury-
causing us occurred (or allegedly occurred) in Tetravue’s own “advertising”

1 of its “products”, its “work” or “completed work” during the policy
2 period(s).

3 (*Id.* ¶ 12, Ex. 10 at 262, emphasis added.) On March 23, Vantress responded by accusing
4 Collins of “mak[ing] the same mistakes we wrote to you about before” and having
5 “almost a complete lack of understanding of both the allegations in the Cross-complaint
6 as well as your duties under the law.” (*Id.* Ex. 11 at p. 264.) Absent, however, was any
7 reference to allegations suggesting the cross-action involved GA’s “advertising material.”
8 It is reasonable to infer that Vantress’s failure to do so was because similar to Collins and
9 St. Paul, Plaintiffs were unaware of any allegations supporting such an inference.

10 Similarly, Plaintiffs’ Declaratory Relief Complaint also indicates that Plaintiffs
11 were unaware of allegations supporting an inference that GA used the subject material in
12 its advertising. Although Plaintiffs explicitly alleged that GA’s Amended Cross-
13 Complaint “makes numerous references to the advertising activities of the *insured*” (*Dec.*
14 *Relief Compl.* ¶ 16, emphasis added), the Declaratory Relief Complaint did not allege the
15 cross-action involved GA’s advertising material or activities (*id.*). The absence of any
16 such allegation in Plaintiffs’ pleading also supports the inference that Plaintiffs were
17 unaware of any such factual allegations in GA’s Amended Cross-Complaint.

18 Similarly, there is also no dispute that in the Declaratory Relief Action, the
19 Superior Court granted St. Paul’s summary-judgment motion, agreeing with St. Paul’s
20 interpretation of GA’s Amended Cross-Complaint. Specifically, the court found that
21 while GA was alleging *Plaintiffs*

22 may be seeking customers or increasing sales with property taken from GA,
23 the *property taken from GA was not advertising material* because the
24 allegations are that the property was trade secret or confidential information.
25 As such, *it is not used by GA* to attract attention in seeking customers or
increasing sales so the Advertising Injury coverage does not apply.

26 (*Brooks Decl.* Ex. 20 at p. 26, emphasis added.) Although the Superior Court’s decision
27 is not “presumptive evidence” of a lack of bad faith, the court’s objective assessment is
28 further evidence that St. Paul’s position was, at best, reasonable or, at worst, an honest

1 mistake or bad judgment, neither of which are sufficient to constitute bad faith. See
2 Wilson, 45 Cal.4th at 722.

3 Nor does the Court of Appeal’s decision demonstrate St. Paul acted in bad faith.
4 Because the Amended Cross-Complaint did not explicitly allege Banks took GA’s
5 advertising material, the court’s finding was based on factual inferences, drawn from a
6 relatively small number of factual allegations, buried in the “187 charging paragraphs”
7 discussing “high level technology.” (*Ct. App. Decision* p. 18.⁷) Moreover, unlike
8 Collins, by the time the Court of Appeal began its coverage analysis, the parties focused
9 the court on the specific issue of whether the cross-action involved GA’s advertising
10 material or activities. (*Id.* p.16, n. 3.) In contrast, when Collins began evaluating
11 coverage, the parties were initially focused on coverage under the policy’s property-
12 damage provision, before turning to the advertising-injury provision. Under these
13 circumstances, the Court of Appeal’s decision does not support an inference that St. Paul
14 acted consciously and deliberately to frustrate Plaintiffs’ expectations.⁸ See Wilson, 42
15 Cal.4th at 726.

16 In sum, there is no evidence suggesting St. Paul’s failure to draw the same
17 inferences and conclusion as the Court of Appeal constituted bad faith. To the contrary,
18 the undisputed fact that Plaintiffs and the San Diego Superior Court also did not draw the
19 same inferences and conclusion as the Court of Appeals supports the finding that St.
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22 ⁷ The Court recognizes that the Court of Appeal’s decision states that “many of the allegations are
23 sufficient to create a reasonable inference that [GA] used some of the materials” for advertising. (*Ct.*
24 *App. Decision* p. 18.) But the court then cites only two allegations supporting this inference (*id.* p. 18),
25 and only four allegations supporting the inference that some of the materials Banks took were not for
internal purposes and thus might have been used to attract the attention of others (*Id.* pp. 19–21).

26 ⁸ Plaintiffs’ opposition discusses 13 facts they contend “support the conclusion that St. Paul acted
27 unreasonably and without proper cause, resulting in a record upon which summary judgment cannot be
28 granted[.]” (*Pls’ Opp’n* 3:9–10.) The primary problem with Plaintiffs’ argument is that the 13 facts
provide no insight into whether St. Paul’s belief that the cross-action did not involve Banks’ theft of GA
advertising material was unreasonable and made without proper cause.

Paul's failure to do so was reasonable. Accordingly, St. Paul is entitled to summary adjudication of Plaintiffs' bad-faith claim.

B. Damage Claims

1. Bad faith, punitive damages and *Brandt* fees.

St. Paul argues Plaintiffs are not entitled to (1) bad-faith damages while the San Diego Superior Court's judgment was in effect, (2) punitive damages, and (3) attorneys' fees under Brandt v. Superior Court, 37 Cal. 3d 813 (1985).⁹ (*Defs' MSJ* 23:16–24:3, 25:15–26:13, 29:24–31:13.) Because the Court has found the undisputed evidence does not support Plaintiffs' bad-faith claim, Plaintiffs cannot recover these damages.

2. Value of Banks' time.

St. Paul seeks summary adjudication on Plaintiffs' damage claim for the value of Banks' time spent helping his attorneys defend GA's cross action. (*Def's P&A* 28:14–18.) Plaintiffs contend these damages are recoverable as contract damages, and that "economic loss of this type may also be recovered in a tort action for breach of the duty of good faith and fair dealing." (*Pls' Opp'n* 23:27–24:1.)

In Richards v. Sequoia Ins. Co., 195 Cal. App. 4th 431 (2011), the California Court of Appeal held that insureds, who were attorneys, were not entitled to recover as damages the value of their time spent defending a lawsuit. *Id.* at 437–438. According to the court, the "measure of damages for any breach of the insurer's contractual duty to defend are the 'costs and attorney's fees *expended* by the insured in defending the underlying action.'" *Id.* at 437 (citing Emerald Bay Community Assn. v. Golden Eagle Ins. Corp., 130 Cal. App. 4th 1078, 1088–1089 (2005) (emphasis added)). Relying on the California Supreme Court's decision in Trope v. Katz, 11 Cal. 4th 274 (1995), the court explained

⁹ Under Brandt, an insured is entitled to recover attorneys' fees incurred to recover policy benefits where the insurer acted in bad faith. *Id.* 37 Cal. 3d at 819.

1 that compensation for the insured's time spent self-representing in the underlying case
2 did not constitute "the payment of 'attorney's fees expended by the insured.'" *Id.* at 437.
3 Similarly, Banks' time spent helping his attorneys defend the cross-action does not
4 constitute the payment of attorneys' fees. Accordingly, Banks is not entitled to recover
5 the value of his time as contract damages.

6 With respect to Plaintiffs' contention that these damages are recoverable in tort,
7 because St. Paul is entitled to summary adjudication of the bad-faith claim, Plaintiffs
8 cannot recover the value of Banks' time under a tort theory.

9 10 **3. Loss of project funding.**

11 St. Paul seeks summary adjudication on Plaintiffs' damage claim for loss of project
12 funding on the basis that those damages were neither expected nor contemplated by either
13 party when the policy was issued. (*Def's P&A* 29:4–14.) Plaintiffs oppose by arguing
14 that whether the parties contemplated those damages depends on disputed issues of
15 material fact. (*Pls' Opp'n* 22:23–23:8.)

16 In support of its motion, St. Paul relies on California Shoppers, Inc. v. Royal Globe
17 Ins. Co., 175 Cal. App. 3d 1 (1985), which evaluated whether the insured, California
18 Shoppers, was entitled to \$3 million in damages for economic or business loss arising
19 from its insurer's, Royal Globe's, breach of the duty to defend. *Id.* at 13, 58–59.
20 California Shoppers asserted that because Royal Globe wrongfully refused to provide a
21 defense, California Shoppers was prematurely "forced" to sell its assets for far less than it
22 could have obtained had the sale been postponed. *Id.* at 61–62. In evaluating the claim,
23 the court explained that "measuring the scope of recoverable damages in breach of
24 contract cases must be restricted to such damages as were actually contemplated by or
25 within the reasonable contemplation of the parties at the time they entered into the
26 contract." *Id.* at 59. According to the court, "this measure, i.e., 'within the reasonable
27 contemplation of the parties,' [citation omitted] is something much more limited in scope
28 than that applied in tort cases where the fiction of foreseeability of the risk is one of many

1 factors woven into the complicated fabric which finally is labeled proximate cause in
2 such cases.” Id. Applying this rule, the court reasoned:

3 To bring the award of \$3 million of *consequential* damages resulting from
4 the breach of the duty to defend within the measure of damages rule we have
5 recited, it would be necessary to hold that the parties contemplated, *at the*
6 *time the insurance was purchased*, that: (1) California Shoppers would
7 violate the Unfair Practices Act; (2) a competitor would sue California
8 Shoppers because of such violations; (3) Royal Globe would decline
9 coverage and the tender of this defense; (4) because of \$39,000 in attorney's
10 fees incurred to defend the action, California Shoppers would be forced to
11 sell the publishing enterprise for \$1.5 million; and (5) *Royal Globe was*
12 *aware of California Shoppers' long-range plan to sell the business at a later*
13 *date after it had greatly appreciated in value.* [¶] The mere recital of the
14 requisite combination of items the parties would have had to have in mind to
15 justify this award of damages demonstrates that they could not have been
16 awarded as consequential damages for breach of the contractual duty to
17 defend.

18 Id. at 60 (emphasis in original; footnote omitted).

19 Plaintiffs attempt to distinguish California Shoppers by asserting there exists a
20 disputed issue of material fact regarding whether the parties contemplated Plaintiffs’ loss
21 of project funding when the policy was purchased. (*Pls’ Opp’n* 12:1–8.) But Plaintiffs
22 have failed to provide evidence supporting their argument.

23 St. Paul has provided evidence that the parties did not contemplate Plaintiffs’ loss
24 of project funding when the policy was purchased. Specifically, St. Paul attached Banks’
25 deposition testimony, wherein he admitted that before purchasing the policy, he did not
26 deal with anyone at St. Paul, only an insurance broker, and that he never mentioned the
27 National Science Foundation project, IARPA project or the related Army contract to the
28 broker. (*Brooks Decl.*, Ex. 29 at 098.) Banks further confirmed that he “wouldn’t know”
if St. Paul had “any reason to know, when it issued you the policy, that you had contracts
or grants with the National Science Foundation or IARPA or the U.S. Army.” (*Id.*)

In contrast to St. Paul’s evidence, Plaintiffs have provided no evidence remotely
indicating the parties contemplated Plaintiffs’ loss of project funding when the policy was

1 purchased. Because the only evidence before the Court indicates the parties did not
2 contemplate Plaintiffs' loss of project funding, there are no disputed issues of fact and St.
3 Paul is entitled to summary adjudication of this damage claim.

4
5 **V. DISCUSSION - PLAINTIFFS' MOTION**

6 **A. The Buss Reimbursement Claim.**

7 Plaintiffs seek summary adjudication of St. Paul's claim for reimbursement under
8 Buss v Superior Court, 16 Cal. 4th 35 (1997). Plaintiffs contend St. Paul cannot prevail
9 on its counterclaim for three reasons: (1) the claim is precluded by the Court of Appeal's
10 decision that there was potential coverage under the advertising-injury-liability provision;
11 (2) based on its discovery responses, St. Paul cannot offer evidence supporting its claim;
12 and (3) the claim is precluded under California law because St. Paul did not provide a
13 defense while the underlying case was ongoing. (*Pls' P&A* [Doc. 65-1]1:10–19.)

14
15 **1. The Court of Appeal's decision does not preclude reimbursement.**

16 Plaintiffs argue the Court of Appeal's decision precludes St. Paul's reimbursement
17 claim. According to Plaintiffs, the advertising-injury allegations that led the court to find
18 a potential for coverage were all found in the first 125 paragraphs of GA's Amended
19 Cross-Complaint. (*Pls' P&A* 7:20–24.) Because those paragraphs are expressly
20 incorporated by reference into each and every one of the seven causes of action asserted
21 against Plaintiffs, they contend there was necessarily a potential for coverage under each
22 cause of action. (*Id.* 7:26–28.) The Court is not persuaded for two reasons.

23 First, Plaintiffs' argument is premised on the idea that the Court of Appeal
24 determined that there was potential coverage under all of the causes of action in the
25 Amended Cross-Complaint. But the Court is unaware of, and Plaintiffs have not pointed
26 to, any language in the decision finding potential coverage under all of GA's claims.
27 Instead, the decision simply found that "the facts alleged reveal *at least a possibility* that
28

1 a claim asserted by General Atomics against Tetravue and Banks *may* have been covered
2 by the Policy....” (*Ct. App. Decision* pp. 22–23, emphasis in original.)

3 Second, as St. Paul points out, Plaintiffs do not cite any authority to support the
4 proposition that GA’s incorporation by reference of the factual allegations creates a
5 potential for coverage under each cause of action. Indeed, Buss cautioned against too
6 much reliance on the pleadings because “[t]he ‘plasticity of modern pleading’ [citation
7 omitted] allows the transformation of claims that are at least potentially covered into
8 claims that are not, and vice versa.” Buss, 16 Cal. 4th at 49. For this additional reason,
9 the Court is not persuaded by Plaintiffs’ argument.

11 **2. The claim is not precluded as a matter of law.**

12 Plaintiffs argue that because St. Paul initially denied coverage and did not agree to
13 pay Plaintiffs’ defense fees until nearly 2 years after the trial ended, St. Paul failed to
14 provide an immediate and entire defense as required by Buss, and therefore is not entitled
15 to reimbursement. (*Pls’ P&A* 12:10–27, 14:14–19.) The Court disagrees.

16 First, Plaintiffs have already raised this argument in opposing St. Paul’s motion for
17 leave to file the counterclaim for Buss reimbursement. In rejecting Plaintiffs’ argument,
18 this Court found that Plaintiffs’ reliance on Buss was misplaced because the case did not
19 attempt to decide the issue presented here: whether an insurer who wrongfully refuses to
20 defend is precluded from reimbursement even if it ultimately pays the insured’s defense
21 costs. (*See Order Granting Motion for Leave to File Counterclaim* [Doc. 35]. 3:4–5.)
22 Moreover, Plaintiff’s reliance on Buss’s statement that an insurer must defend
23 immediately is misplaced because it was in the context of explaining why an insurer must
24 pay all defense costs in a “mixed action,” including those for which there is no potential
25 for coverage.¹⁰ See Buss 16 Cal. 4th at 48–49. Contrary to Plaintiffs’ argument, Buss

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28 ¹⁰ The Order Granting Motion for Leave to File Counterclaim also found that Plaintiffs’ reliance on Buss
was misplaced because the statement that an insurer must defend immediately was in the context of

1 did not establish an insurer's obligation to defend "immediately" as a condition for a
2 reimbursement claim.

3 Second, Plaintiffs' argument that an insurer "is foreclosed from ever seeking
4 reimbursement for costs of defense" when it fails to provide an immediate defense was
5 rejected in State v. Pacific Indemnity Co., 63 Cal. App. 4th 1535, 1550 (1998). Plaintiffs
6 argue that Pacific Indemnity rejection of their argument is dicta. Evening assuming
7 Plaintiffs are correct, the Court finds Pacific Indemnity persuasive for at least two
8 reasons.

9 Plaintiffs have failed to cite any case contradicting Pacific Indemnity's dicta. Nor
10 is the Court aware of any case holding that an insurer is precluded from Buss
11 reimbursement where it wrongfully refuses to defend, but ultimately pays all of the
12 insured's defense costs. At most, the California cases Plaintiffs cite, as well as Pacific
13 Indemnity, establish that in a mixed case, an insurer who wrongfully refuses to defend is
14 not entitled to reimbursement until after it pays all of the insured's defense costs.

15 Additionally, precluding an insurer from seeking reimbursement would undermine
16 the goal that all the parties receive the benefit of the bargain. Under Pacific Indemnity's
17 approach, where a duty to defend is owed, the insured must first receive the benefit of the
18 bargain (i.e., payment of defense expenses) before the insurer is entitled to seek and
19 obtain its benefit of the bargain (i.e., reimbursement for claims where there was no
20 potential coverage). Under this approach, both parties receive the benefit of the bargain.
21 In contrast, under Plaintiffs' theory, only the insured receives the benefit, as well as the
22 windfall of having the insurer pay defense costs for uncovered claims. Absent bad faith,
23 Plaintiffs have not cited authority or provided any rational basis for their position that the
24 insured should receive a windfall, while the insurer is denied the benefit of the bargain.

25
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27
28 explaining when the duty to defend arises. (*See Order Granting Motion for Leave to File Counterclaim*
[Doc. 35] 3:2–4.)

1 **3. St. Paul’s discovery responses.**

2 Plaintiffs also argue that St. Paul cannot prevail on its reimbursement claim
3 because it cannot meet its burden of producing evidence to establish that certain defense
4 costs are attributable solely to an uncovered claim. According to Plaintiffs, during
5 discovery Defendants were “asked to identify all defense costs it paid and which it claims
6 are not attributable solely to claims for which there was not even a potential for coverage,
7 on an item by item basis.” (*Pls’ P&A* 9:18–23.) Rather than allocate defense costs on an
8 item-by-item basis, Defendants asserted that it was entitled to reimbursement for all
9 defense costs because “none of the GA claims had a potential for coverage.” (*Id.* 9:24–
10 27.) Defendants’ position, however, is foreclosed by the Court of Appeal’s finding that a
11 potential for coverage existed under at least one of the causes of action. (*Id.* 9:3–15.)
12 Accordingly, because Defendants did not allocate defense costs on an item-by-item basis,
13 Plaintiffs contend they cannot now provide evidence to defeat summary judgment. (*Id.*
14 9:23–10:6.)

15 As an initial matter, Plaintiffs are correct that the Court of Appeal’s decision
16 constitutes collateral estoppel regarding whether a potential for coverage exists under at
17 least one of the causes of action in GA’s Amended Cross-Complaint. (*See Ct. App.*
18 *Decision* pp. 22–23.) Therefore, any theory by St. Paul that is premised on the ability to
19 establish none of the causes of action gave rise to a potential for coverage lacks merit.

20 Nevertheless, the problem with Plaintiffs’ argument is that the central premise—that
21 St. Paul’s discovery response did not identify specific defense costs attributable to a non-
22 covered claim—is not supported by the evidence. Although St. Paul’s discovery response
23 asserted “that all [GA’s] cross-claims against [Plaintiffs] in the underlying action were
24 not potentially covered...”, St. Paul then identified specific items for which they are
25 seeking reimbursement. (*Sarneky Decl.* Ex. 8 at 149–153.) For example, St. Paul
26 asserted that none of the costs associated with the depositions of Paul Banks, Gregory
27 Leonard, Murray Road, Alan Spero, Richard Abrams, Timothy Bertch, Michael Perry,
28 Robin Snider and Thomas Baur were attributable to potentially covered claims. (*Id.* 150.)

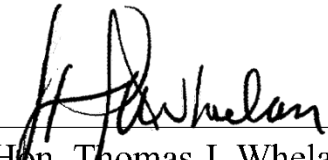
1 Similarly, St. Paul asserted that specific motions were also not related to potentially
2 covered claims. (*Id.* 151–152.) Plaintiffs’ argument is, therefore, not supported by the
3 record because St. Paul has identified specific costs that it may argue at trial are not
4 attributable to a claim for which there was potential coverage.¹¹

5
6 **VI. CONCLUSION & ORDER**

7 For the reasons set forth above, the Court **GRANTS** Plaintiffs’ and Defendant’s
8 motions to file documents under seal [Docs. 66, 73], **DENIES** Plaintiffs’ summary-
9 judgment motion [Doc. 65] and **GRANTS IN PART** and **DENIES IN PART**
10 Defendants’ summary-judgment motion [Doc. 70].¹²

11 **IT IS SO ORDERED.**

12 Dated: March 6, 2018

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15 Hon. Thomas J. Whelan
United States District Judge

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25 ¹¹ Whether St. Paul is limited to seeking reimbursement for only those items specifically identified in
26 response to the interrogatory is beyond the scope of this order.

27 ¹² St. Paul also seeks summary adjudication on two damage claims that Plaintiffs did not identify in their
28 initial Rule 26(a) disclosure. (*Def’s P&A* 26:14–17.) Alternatively, St. Paul has filed a motion in limine
to exclude those damages. (*See Def’s Mt. in Limine* [Doc. 69].) The Court will resolve the issue by
ruling on the motion in limine at the appropriate time.